

ORIGINAL




0000020057

MEMORANDUM

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TO: Docket Control

FROM: Ernest G. Johnson
Director
Utility Division

for 

DATE: April 11, 2005

RE: STAFF REPORT FOR OAK CREEK UTILITY CORPORATION RATE
INCREASE APPLICATION (DOCKET NO. WS-02061A-04-0835) AND
FINANCING (DOCKET NO. WS-02061A-04-0836)

Attached is the Staff Report for Oak Creek Utility Corporation's application for a permanent rate increase. Staff recommends approval of the application using Staff's recommended rates and charges.

EGJ:ENZ:red

Originator: Elena Zestrijan


Attachment: Original and sixteen Copies

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Service List for: Oak Creek Utility Corporation
Docket No. WS-02061A-04-0835 and WS-02061A-04-0836

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**STAFF REPORT
UTILITY DIVISION
ARIZONA CORPORATION COMMISSION**

OAK CREEK UTILITY CORPORATION

**DOCKET NO. WS-02061A-04-0835
DOCKET NO. WS-02061A-04-0836**

**APPLICATION FOR A
PERMANENT RATE INCREASE
AND FINANCING APPLICATION**

APRIL 11, 2005

STAFF ACKNOWLEDGMENT

The Staff Report for Oak Creek Utility Corporation, Docket Nos. WS-02061A-04-0835 and WS-02061A-04-0836 was the responsibility of the Staff members listed below. Elena Zestrijan was responsible for the review and analysis of the Company's application, recommended revenue requirements, rate base and rate design. Dennis R. Rogers was responsible for the review and analysis of the Company's financing application. Lyndon Hammon was responsible for the engineering and technical analysis. John LaPorta was responsible for reviewing the Commission's records on the Company, determining compliance with Commission policies/rules and reviewing customer complaints filed with the Commission.



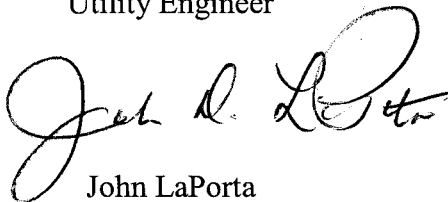
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Public Utility Rate Analyst IV



Lyndon Hammon
Utility Engineer



John LaPorta
Public Utility Consumer Analyst I

**EXECUTIVE SUMMARY
OAK CREEK UTILITY CORPORATION
DOCKET NOS. WS-02061A-04-0835
AND WS-02061A-04-0836**

Oak Creek Utility Corporation ("Company") is engaged in the business of providing utility water and sewer service exclusively to Arizona customers in Coconino County. The Company is located on the east side of Oak Creek, near the old "Indian Gardens" and "sand statues" area, along Highway 89A. The subdivision was originally platted in 1966. The Company presently serves about 31 customers within a 6.63 acre certificated area.

The Company's **water** rate application proposes an increase in revenues of \$18,806 or a 166.29 percent increase over adjusted test year revenues of \$11,309. The Company's proposed rates will produce revenues of \$30,115, an operating income of \$12,454, for a 57.04 percent rate of return on an original cost rate base ("OCRB") of \$21,835. The Company's proposed rates would increase the typical residential bill with a median usage of 2,074 gallons from \$23.19 to \$58.48 for an increase of \$35.29 or 152.20 percent.

The Company's **wastewater** rate application proposes an increase in revenues of \$14,666 or a 209.84 percent increase over adjusted test year revenues of \$6,989. The Company's proposed rates will produce revenues of \$21,655, an operating income of \$11,345, for a 25.03 percent rate of return on an OCRB of \$45,325. The Company's proposed rates would increase the typical residential bill with a median usage of 2,074 gallons from \$17.07 to \$52.26 for an increase of \$35.19 or 206.20 percent.

Staff is recommending an increase in **water** revenues of \$6,228 or a 55.07 percent increase over adjusted test year revenues of \$11,309. Staff's recommended rates will produce revenues of \$17,537, an operating income of \$7,511, for a 21.92 percent rate of return on an OCRB of \$34,268. Staff's recommended rates would increase the typical residential bill with a median usage of 2,074 gallons from \$23.19 to \$36.01 for an increase of \$12.82 or 55.30 percent.

Staff is recommending an increase in **wastewater** revenues of \$3,593 or a 51.41 percent over adjusted test year revenues of \$6,989. Staff's recommended rates will produce revenues of \$10,582, an operating income of \$3,818, for an 11.40 percent rate of return on an OCRB of \$33,505. Staff's recommended rates would increase the typical residential bill with a median usage of 2,074 gallons from \$17.07 to \$24.67 for an increase of \$7.60 or 44.50 percent.

Staff recommends approval of its recommended rates and charges as presented on Schedule 4 of this report.

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Attachments

Financial Report
Engineering Report

FACT SHEET

Current rates: Decision No. 54664, dated August 22, 1985.

Type of ownership: Arizona Sub-Chapter "S" Corporation.

Location: The Company is located on the east side of Oak Creek, near the old "Indian Gardens" and "sand statues" area, along Highway 89A in Coconino County. The subdivision was originally platted in 1966. Oak Creek Utility presently serves about 30 customers within a 6.63 acre certificated area. The Company serves approximately 31 customers. The water system is not located in an Active Management Area ("AMA").

The Company is operating two separate systems, a water system and a wastewater system. Revenues are accounted for separately, however the Company does not keep separate books for the operating expenses incurred.

Rates:

Permanent rate increase application filed December 9, 2004

Current Test Year Ended: December 31, 2003

Current Rates: Effective August 22, 1985

	<u>Current Rates</u>	<u>Company Proposed Rates</u>	<u>Staff Recommended Rates</u>
<u>Water</u>			
Monthly Minimum Charge Based on 5/8 X 3/4 - inch meter	18.00	\$45.00	\$30.00
Gallons in Minimum	0	0	0
Commodity Charge			
Flat Rate per 1,000 Gallons	\$ 2.50	\$ 6.50	N/A
Excess of minimum, per 1,000 gallons:			
From 0 to 3,000 gallons	N/A	N/A	\$ 2.90
From 3,001 to 15,000 gallons	N/A	N/A	\$ 4.00
In excess of 15,001 gallons	N/A	N/A	\$ 5.00
Typical residential bill (Based on median usage of 2,074 gallons)	\$23.19	\$58.48	\$36.01

	<u>Current Rates</u>	<u>Company Proposed Rates</u>	<u>Staff Recommended Rates</u>
<u>Wastewater</u>			
Monthly Minimum Charge			
Measured Rate Customers			
Residential	\$15.00	\$45.00	\$20.00
Commercial	\$45.00	\$45.00	\$55.00
Measured Rate Customers			
Flat Rate per 1,000 Gallons			
Residential	\$ 1.00	\$ 3.50	\$ 2.25
Commercial	\$ 1.00	\$ 3.50	\$ 4.00
Typical residential bill (Based on median usage of 2,074 gallons)	\$17.07	\$52.26	\$24.67

Customers:

Average number of customers in current test year: 31

Current test year customers by meter size: 5/8 X3/4 - inch meter - 31

Complaints:

Number of customer concerns since rate application filed: 13

Percentage of concerns to customer base: 42 percent

Notification:

Customer notification was mailed on December 22, 2004.

Summary of Filing

Based on test year results as adjusted by Utility Division Staff ("Staff"), Oak Creek Utility Corporation ("Company"), **Water Division** realized an operating income of \$1,333 on an original cost rate base ("OCRB") of \$34,268 for a rate of return of 3.89 percent as shown on Schedule W-1.

Based on test year results as adjusted by Staff the Company **Wastewater Division** realized an operating income of \$417 on an OCRB of \$33,505 for a rate of return of 1.24 percent as shown on Schedule WW-1.

The Company's **Water Division** proposed rates that would produce operating revenues of \$30,115 and an operating income of \$12,454 for a 57.04 percent rate of return on an OCRB of \$21,835. The Company's proposed rates would increase the typical residential bill with a median usage of 2,074 gallons from \$23.19 to \$58.48 for an increase of \$35.29 or 152.20 percent.

Staff's recommended **water** rates would produce operating revenues of \$17,537 and an operating income of \$7,511 for a 21.92 percent rate of return on an OCRB of \$34,268. Staff's recommended rates would increase the typical residential bill with a median usage of 2,074 gallons from \$23.19 to \$36.01 for an increase of \$12.82 or 55.30 percent.

The Company's **Wastewater Division** proposed rates that would produce operating revenues of \$21,655 and an operating income of \$11,345 for a 25.03 percent rate of return on an OCRB of \$45,325. The Company's proposed rates would increase the typical residential bill with a median usage of 2,074 gallons from \$17.07 to \$52.26 for an increase of \$35.19 or 206.20 percent.

Staff's recommended **wastewater** rates would produce operating revenues of \$10,582 and an operating income of \$3,818 for an 11.40 percent rate of return on an OCRB of \$33,505. Staff's recommended rates would increase the typical residential bill with a median usage of 2,074 gallons from \$17.07 to \$24.67 for an increase of \$7.60 or 44.50 percent.

Background

On December 9, 2004, the Company filed an application for a permanent rate increase with the Arizona Corporation Commission ("Commission"). The application was found deficient. After the Company filed corrections to its application, the application was deemed sufficient on February 9, 2005. The Company served approximately 31 customers in the test year.

The Company indicated that a rate increase is needed because it has not requested rate increases in the last nineteen years.

The Company separately filed an application requesting authority to borrow \$40,000 from the Water Infrastructure Finance Authority ("WIFA"). On March 17, 2005, the Company filed a motion to consolidate the rate case and the financing case. Staff did not oppose the consolidation motion.

Staff recommends authorization to obtain \$40,000 of long-term debt financing on the terms and conditions consistent with, or better than, those used in Staff's pro forma analysis subject to establishment of rates that provide Staff's recommended operating income.

Consumer Services

A review of the Commission's records found that the Company has a backflow/cross connection tariff on file. Staff recommends that the Company file an amended curtailment tariff to include key language omitted on its initial filing. The Company's customer bill is in compliance with the Arizona Administrative Code R14-2-409 B.2. Thirteen opinions were filed as a result of the current rate increase application. The opinions received were against the Company proposed rate increase.

Engineering Analysis

Staff inspected the Company's plant facilities on May 25, 2004. A complete discussion of Staff engineering findings, recommendations, and description of the water system is provided in the attached Engineering Report.

Water testing expense is based upon, participation in the Arizona Department of Environmental Quality ("ADEQ") Monitoring Assistance Program. Annual testing expense was, adjusted to an annual expense of \$712 as described in the Engineering Report, page 5.

Staff recommends that the Company change its depreciation rates to specific depreciation rates for the National Association of Regulatory Utility Commissioners ("NARUC") plant equipment categories as shown in Exhibit 3A Water and 3B Wastewater of the attached Engineering Report.

The Company's **water** system consists of one well, which directly pressurizes a hydro-pneumatic tank and distribution mains. For details on water system production and ADEQ requirements, see Engineering Report, page 3, Financing. Based on Staff's analysis, the Company's water loss is 13.5 percent.

Non-account water should be 10% or less and never more than 15%. It is important to be able to reconcile the difference between water sold and the water produced by the source. A water balance will allow a water company to identify water and revenue losses due to leakage, theft, and flushing. Unfortunately, the monthly non-account water was ambiguous and varied from a 77% loss to a 133% gain.

One possible explanation may involve the location of the well meter. A totalizing turbine well meter usually works best in an application where the flows are relatively constant. In other words, the well pump turns on and pumps at a fairly constant rate through the turbine meter, and then turns off. At Oak Creek, the well meter is located on the demand side of the pressure tank. Flows vary according to the water system demand and can fluctuate from zero to a maximum system demand. Under this condition, a turbine meter would typically read low at low flows. This would result in a situation where water pumped would be less than water sold, which is the exact circumstance in this case.

The storage tank project offers an ideal time to fix the metering problem since the well piping will be reconfigured during the storage tank construction. Therefore, Staff recommends that the existing well meter shall be relocated, or as an alternative, a new well meter shall be installed between the well discharge and the storage tank, or in such a location to best conform to the manufacturer's recommended location and manufacturer's recommended function.

The Company's **wastewater** system consists of a collection system, which drains to a small pumping station. The sewage is then pumped to a community septic tank and leach field.

Compliance

Utility Division Compliance Unit showed no outstanding compliance issues.

The Company is not within an AMA and is not subject to the Arizona Department of Water Resources ("ADWR") monitoring and reporting requirements for groundwater withdrawals.

Water- ADEQ reported that the Company is delivering water, which meets the standards required by the Arizona Administrative Code, Title 18 Chapter 4. Although no water quality problems were reported, ADEQ identified two major operation and maintenance deficiencies. Those deficiencies were the lack of a one-day's minimum storage and the lack of an approved microbiological site sampling plan. A microbiological site sampling plan is required by State rule and is intended to insure that the procedure, quantity, and location of coliform sampling will truly represent the biological quality within a water distribution system. Because of this potential public health risk, Staff recommends that the Company submit evidence of an ADEQ approved microbiological site sampling plan before new rates become effective in this case. For more details see attached Engineering Report.

Wastewater – System consists of a simple septic tank and subsurface disposal system for the effluent. Under ADEQ permit rules, septic tank systems of certain sizes and disposal densities are treated differently from more sophisticated bio-mechanical systems. The Company filed with ADEQ, a "Notice of Disposal" which should qualify them for a general permit. ADEQ confirmed that the facility has a General Permit in good standing in accordance with its aquifer protection rules, and that no monitoring or reporting is required at this time.

Arsenic - Water

The U.S. Environmental Protection Agency ("EPA") will reduce the arsenic maximum contaminant level ("MCL") in drinking water from 50 micrograms per liter (" $\mu\text{g/l}$ ") to 10 on January 23, 2006. The most recent laboratory analysis indicates that the arsenic level is 8.7 $\mu\text{g/l}$. Based on this data, the Company is in compliance with the new arsenic MCL.

Rate Base - Water

As shown on Schedule W-2, page 1, Staff recommends a rate base of \$34,268. This rate base represents an increase of \$12,434 from the Company's proposed \$21,835 rate base, primarily due to Staff's adjustment to accumulated depreciation.

Adjustment A as shown in Schedule W-2, page 1, decreased plant in service by \$5,263, based on Staff's analysis.

Adjustment B as shown in Schedule W-2, page 1, decreased accumulated depreciation by \$18,375, due to Staff's calculation using approved depreciation rates for the intervening years since the prior rate case.

Adjustment C reflects a reduction in operating and maintenance cash working capital component of \$678 due to Staff adjustments to operating expense.

Rate Base - Wastewater

As shown on Schedule WW-2, page 1, Staff recommends a rate base of \$33,505. This rate base represents a decrease of \$11,820 from the Company's proposed \$45,325 rate base, due to Staff's adjustment to plant in service and accumulated depreciation.

Adjustment A as shown in Schedule WW-2, page 1, decreased plant in service by \$52,606, based on Staff's analysis.

Adjustment B as shown in Schedule WW-2, page 1, decreased accumulated depreciation by \$41,084, due to Staff's calculation using approved depreciation rates for the intervening years since the prior rate case.

Adjustment C reflects a reduction in operating and maintenance cash working capital component of \$298 due to Staff adjustments to operating expense.

Operating Revenues - Water

Staff has not adjusted the revenues.

Operating Revenues - Wastewater

Staff has not adjusted the revenues.

Operating Expenses - Water

Staff adjustments to operating expenses resulted in a decrease of \$7,685 from \$17,661 to \$9,976, as shown on Schedule WW-3, page 1. The adjustments are discussed below.

Adjustment A adjusts the Company's application amount which reflected a 10-year average. Staff removed the highest and lowest years and used a truncated average of eight years, at 65 percent allocated expense to the water division and 35 percent to the wastewater division. This adjustment reduced repairs and maintenance by \$1,333.

Adjustment B decreased outside services by \$505. Staff's adjustment is based on the Company's general ledger actual expense allocated at 65 percent to the water division and 35 percent to the wastewater division.

Adjustment C decreased water testing. Staff decreased Company's testing expense to Staff's recommended amount of \$712.

Adjustment D reflects Staff's removal of rent expense in the amount of \$150. Company's general ledger rent account carries a zero balance. Staff submitted a data request and an e-mail to the Company's Counsel requesting clarification, account number or canceled checks covering rent expense, but Staff was unable to obtain requested clarification.

Adjustment E decreased rate case expense by \$350 to reflect 65 percent of the expense allocated to the water division and 35 percent allocation to the wastewater division.

Adjustment F decreased miscellaneous expense, by \$1,815 to reflect Company's actual expense as it appears in the general ledger. Staff received no response to data requests seeking clarification.

Adjustment G decreased depreciation expense by \$2,258 to reflect the appropriate expense based on Staff's calculation using Staff recommended rates.

Operating Expenses - Wastewater

Staff adjustments to operating expenses resulted in a decrease of \$3,738 from \$10,310 to \$6,572, as shown on Schedule WW-3, page 1. The adjustments are discussed below.

Adjustment A adjusts the Company's application amount which reflected a 10-year average. Staff removed the highest and lowest years and used a truncated average of eight years,

at 35 percent allocated expense to the wastewater division and 65 percent to the water division. This adjustment reduced repairs and maintenance by \$23.

Adjustment B increased office supplies by \$501. Staff's adjustment reflects 35 percent of the incurred expense recorded on Company's general ledger and lack of Company response to Staff data requests.

Adjustment C increased contractual services professional by \$1,202. Staff's adjustment reflects 35 percent of the incurred expense recorded on Company's general ledger and lack of Company response to Staff data requests.

Adjustment D removed contractual services testing. Staff removed Company's testing expense. The Company is on a community septic tank and the general permit does not require a fee.

Adjustment E reflects Staff's removal of contractual services other. The Company is on a community septic tank and minimum maintenance is required. Staff's allocated expense, to the contractual services professional category, reflect management company's billing fees.

Adjustment F reflects Staff's removal of rent expense in the amount of \$150. Company's general ledger rent account carries a zero balance. Staff submitted a data request and an e-mail to the Company's Counsel requesting clarification, general ledger account number, showing entries or canceled checks covering rent expense, but Staff was unable to obtain requested clarification.

Adjustment G decreased rate case expense by \$650 to reflect 35 percent of the expense incurred to the wastewater division, the other 65 percent pertains to the water division.

Adjustment H decreased miscellaneous expense, by \$274 to reflect Company's actual expense as it appears in the general ledger.

Adjustment I decreased depreciation expense by \$214 to reflect the appropriate expense based on Staff's calculation.

Rate of Return - Water

The Company proposed rates and charges result in a 57.04 percent rate of return on the Company's rate base of \$21,835. This rate of return would provide a positive cash flow of approximately \$15,805 and a 41.35 percent operating margin.

Staff's recommended rates and charges result in a 21.92 percent rate of return on the OCRB of \$34,268. This rate of return would provide a positive cash flow of approximately \$8,253 and a 42.83 percent operating margin.

Rate of Return - Wastewater

The Company proposed rates and charges result in a 25.03 percent rate of return on the Company's rate base of \$45,325. This rate of return would provide a positive cash flow of approximately \$13,729 and a 52.39 percent operating margin.

Staff's recommended rates and charges result in an 11.40 percent rate of return on the OCRB of \$33,505. This rate of return would provide a positive cash flow of approximately \$6,180 and a 36.08 percent operating margin.

Revenue Requirements - Water

The Company proposed an increase in revenues of \$18,806 or 166.29 percent over adjusted test year revenues of \$11,309. This increase would result in a rate of return of 57.04 percent and an operating margin of 41.35 percent.

Staff recommended an increase in revenues of \$6,228 or 55.07 percent over adjusted test year revenues of \$11,309. This increase would result in a rate of return of 21.92 percent and an operating margin of 42.83 percent. Staff believes its recommended revenues would allow the Company to meet its obligations and provide a cushion for contingencies.

Revenue Requirements - Wastewater

The Company proposed an increase in revenues of \$14,666 or 209.84 percent over adjusted test year revenues of \$6,989. This increase would result in a rate of return of 25.03 percent and an operating margin of 52.39 percent.

Staff recommended an increase in revenues of \$3,593 or 51.40 percent over adjusted test year revenues of \$6,989. This increase would result in a rate of return of 11.40 percent and an operating margin of 36.08 percent. Staff believes its recommended revenues would allow the Company to meet its obligations and provide a cushion for contingencies.

Rate Design - Water

The Company's current and proposed rate structure consists of a monthly minimum with no gallons in the monthly minimum charge and one commodity rate. Staff's recommended rate design consists of three tiers in the commodity rates and no gallons included in the monthly minimum charge. Staff recommended a first tier break at 3,000 gallons, the second tier break at 15,000 gallons, and the third tier applies to consumption in excess of 15,000 gallons.

The residential customer class served through a 5/8 x 3/4-inch meter is 100 percent of the total water sold.

Staff's recommended rate design set the first tier break at 3,000 gallons. This tier would apply to 63.37 percent of the residential bills that used 15.37 percent of the water sold. The second tier at the 15,000 gallon range would apply to 33.69 percent of the bills which consumed 56.64 percent of the water sold. The third tier in excess of 15,000 gallons would apply to 2.94 percent of the bills that consumed 13.79 percent of the water sold in the residential customer class.

Rate Design - Wastewater

The Company's current and proposed rate structure consists of a monthly minimum with no gallons in the monthly minimum charge and one commodity rate based on water usage. Both the minimum charge and the commodity charge are higher for commercial users, but Staff notes that the Company does not have any commercial customers.

Staff's recommended rate design uses the same methodology as the Company in using a monthly minimum with no gallons and one commodity rate based on water usage. Staff's rates are designed to recover its recommended revenue requirement.

Staff Recommendations

Staff recommends approval of its recommended rates and charges as presented on Schedule W-4 and WW-4 of this report.

Staff further recommends the Company adopt the depreciation rates shown on Exhibit 3 of the attached Engineering Report.

Staff recommends authorization to obtain \$40,000 of long-term debt financing on the terms and conditions consistent with, or better than, those used in Staff's pro forma analysis. This recommendation is conditioned on the establishment of rates that provide Staff's recommended revenue requirement.

Staff recommends that the Company be ordered to maintain separate books in accordance with the NARUC Uniform System of Accounts for water utilities and for wastewater utilities. Staff recommends the Company not be allowed to file any future rate case with expenses allocated between divisions.

Staff further recommends that the Company docket an amended curtailment tariff within 30 days after the effective date of any decision and order pursuant to this application and that the amended curtailment shall contain the following provision:

"If a customer believes he/she has been disconnected in error, the customer may contact the Commission's Consumer Services Section at 1-800-222-7000 to initiate an investigation"

Staff further recommends that the proposed order in this matter shall contain the following two directives to the Company:

1. Oak Creek Utility Corporation shall notify its customers of this new curtailment tariff as part of its next regularly scheduled billing after the effective of the curtailment tariff but no later than sixty (60) days after the effective date of the tariff, and
2. Oak Creek Utility Corporation shall provide a copy of the curtailment tariff to any customer, upon request.

Staff further recommends that the Company docket with the Commission a tariff schedule of its approved rates and charges, within 30 days after the decision in this matter is issued. This tariff schedule should not be modified or changed and it should appear in the same format as ordered by this Commission.

Staff further recommends that, in addition to the collection of the Company's regular rates and charges, the Company shall collect from its customers their proportionate share of any privilege, sales or use tax as provided for in A.A.C. R14-2- 409(D).

Staff further recommends that a 10,000 gallon storage tank project shall be completed within 18 months after the effective date of any decision and order pursuant to this application. The Company shall submit the ADEQ Approval of Construction to Docket Control within 18 months of the effective date of this decision.

Staff further recommends that the existing well meter shall be relocated, or as an alternative, a new well meter shall be installed between the well discharge and the storage tank, or in such a location to best conform to the manufacturer's recommended location and manufacturer's recommended function.

Staff further recommends that any permanent rates and charges in this matter shall become effective on the first day of the month after the Director of the Utilities Division receives notice from the Arizona Department of Environmental Quality that Oak Creek Utility Corporation has an approved microbiological site sampling plan.

SUMMARY OF FILING

	-- Present Rates --		-- Proposed Rates --	
	Company as Filed	Staff as Adjusted	Company as Filed	Staff as Adjusted
Revenues:				
Metered Water Revenue	\$10,058	\$10,058	\$25,790	\$16,286
Unmetered Water Revenue	0	0	3,074	0
Other Water Revenues	1,251	1,251	1,251	1,251
Total Operating Revenue	\$11,309	\$11,309	\$30,115	\$17,537
Operating Expenses:				
Operation and Maintenance	\$13,907	\$8,481	\$13,907	\$8,481
Depreciation	3,351	1,092	3,351	1,142
Property & Other Taxes	403	403	403	403
Income Tax	0	0	0	0
Total Operating Expense	\$17,661	\$9,976	\$17,661	\$10,026
Operating Income/(Loss)	(\$6,352)	\$1,333	\$12,454	\$7,511
Rate Base O.C.L.D.	\$21,835	\$34,268	\$21,835	\$34,268
Rate of Return - O.C.L.D.	-29.09%	3.89%	57.04%	21.92%
Times Interest Earned Ratio (Pre-Tax) *	N/A	N/A	N/A	N/A
Debt Service Coverage Ratio (Pre-Tax) *	N/A	N/A	N/A	N/A
Operating Margin	-56.17%	11.78%	41.35%	42.83%

* TIER and DSC ratios are reflected on Schedule DRR-1 which reflects the effect of the \$40,000 WIFA loan at 6 percent on the combined water and wastewater division totals.

RATE BASE

	----- Original Cost -----		
	Company	Adjustment	Staff
Plant in Service	\$64,809	(\$5,263) (A)	\$59,546
Less:			
Accum. Depreciation	42,886	(18,375) (B)	24,511
Net Plant	\$21,923	\$13,112	\$35,035
Less:			
Advances in Aid of Construction	\$910	\$0	\$910
Meter Deposits (Meter & Service Line)	871	0	871
Total Advances	\$1,781	\$0	\$1,781
Contributions Gross	\$0	\$0	\$0
Less:			
Amortization of CIAC	0	0	0
Net CIAC	\$0	\$0	\$0
Total Deductions	\$1,781	\$0	\$1,781
Plus:			
1/24 Power	\$23	\$0	\$23
1/8 Operation & Maint.	1,670	(678) (C)	992
Inventory	0	0	0
Prepayments	0	0	0
Total Additions	\$1,693	(\$678)	\$1,014
Rate Base	\$21,835	\$12,434	\$34,268

Explanation of Adjustment:

- A - See Schedule W-2, page 2 of 3.
- B - See Schedule W-2, page 3 of 3.
- C - Based on Staff adjustments to operating expenses.

PLANT ADJUSTMENT

	Company Exhibit	Adjustment	Staff Adjusted
301 Organization	\$172	(\$172)	\$0
302 Franchises	0	0	0
303 Land & Land Rights	10,000	20,000	30,000
304 Structures & Improvements	600	266	866
307 Wells & Springs	11,000	(7,015)	3,985
311 Pumping Equipment	10,543	(6,913)	3,630
320 Water Treatment Equipment	0	0	0
330 Distribution Reservoirs & Standpipes	4,000	(515)	3,485
331 Transmission & Distribution Mains	25,000	(14,450)	10,550
333 Services	1,944	1,781	3,725
334 Meters & Meter Installations	600	2,705	3,305
335 Hydrants	0	0	0
336 Backflow Prevention Devices	0	0	0
339 Other Plant and Misc. Equipment	0	0	0
340 Office Furniture & Equipment	950	(950)	0
341 Transportation Equipment	0	0	0
343 Tools Shop & Garage Equipment	0	0	0
344 Laboratory Equipment	0	0	0
345 Power Operated Equipment	0	0	0
346 Communication Equipment	0	0	0
347 Miscellaneous Equipment	0	0	0
348 Other Tangible Plant	0	0	0
105 C.W.I.P.	0	0	0
TOTALS	\$64,809	(\$5,263) (A)	\$59,546

(A) Adjustments based on Staff Engineer's analysis.

ACCUMULATED DEPRECIATION ADJUSTMENT

	<u>Amount</u>
Accumulated Depreciation - Per Company	\$ 42,886
Accumulated Depreciation - Per Staff	24,511
Total Adjustment	<u>\$ (18,375)</u>

Explanation of Adjustment:

B - Accumulated depreciation balance per Staff Engineer, as of December 31, 2002	\$ 23,419
Plus: Depreciation expense 2003	<u>1,092</u>
Staff balance as of December 31, 2003	<u><u>24,511</u></u>

Oak Creek Utility Corporation - Water

Docket No. WS-02061A-04-0835

Test Year Ended December 31, 2003

Schedule W-3

Page 1 of 3

STATEMENT OF OPERATING INCOME

	Company Exhibit	Staff Adjustments	Staff Adjusted
Revenues:			
461 Metered Water Revenue	\$10,058	\$0	\$10,058
460 Unmetered Water Revenue	0	0	0
474 Other Water Revenues	1,251	0	1,251
Total Operating Revenue	\$11,309	\$0	\$11,309
Operating Expenses:			
601 Salaries and Wages	\$0	\$0	\$0
610 Purchased Water	0	0	0
615 Purchased Power	549	0	549
618 Chemicals	0	0	0
620 Repairs and Maintenance	1,972	(1,333) (A)	639
621 Office Supplies & Expense	926	0	926
630 Outside Services	4,508	(505) (B)	4,003
635 Water Testing	1,985	(1,273) (C)	712
641 Rents	150	(150) (D)	0
650 Transportation Expenses	99	0	99
657 Insurance - General Liability	0	0	0
659 Insurance - Health and Life	0	0	0
665 Rate Case Expense	1,000	(350) (E)	650
675 Miscellaneous Expense	2,718	(1,815) (F)	903
403 Depreciation Expense	3,351	(2,259) (G)	1,092
408 Taxes Other Than Income	0	0	0
408.11 Property Taxes	403	0	403
409 Income Tax	0	0	0
Total Operating Expenses	\$17,661	(\$7,685)	\$9,976
OPERATING INCOME/(LOSS)	(\$6,352)	\$7,685	\$1,333
Other Income/(Expense):			
419 Interest and Dividend Income	\$0	\$0	\$0
421 Non-Utility Income	0	0	0
427 Interest Expense	16	0	16
426 Miscellaneous Non-Utility Expense	0	0	0
Total Other Income/(Expense)	(\$16)	\$0	(\$16)
NET INCOME/(LOSS)	(\$6,368)	\$7,685	\$1,317

STAFF ADJUSTMENTS

(A) -	REPAIRS AND MAINTENANCE - Per Company	\$1,972	
	Per Staff	639	(\$1,333)

To correct Company's 10-year average, Staff removed highest and lowest years, and used the truncated average of eight years. Staff allocated 65% of the eight-year average expense to the water division and 35% to the wastewater division.

(B) -	OUTSIDE SERVICES - Per Company	4,508	
	Per Staff	4,003	(\$505)

Staff removed the proforma adjustments that the Company failed to document and to adjust to a 65% allocation of actual expenses.

(C) -	WATER TESTING - Per Company	\$1,985	
	Per Staff	712	(\$1,273)

To record Staff Engineer's recommended water testing expense.

(D) -	RENTS - Per Company	\$150	
	Per Staff	0	(\$150)

To remove unsubstantiated entry.

(E)	RATE CASE EXPENSE - Per Company	1,000	
	Per Staff	650	(\$350)

65% allocation to the Water division.

(F)	MISCELLANEOUS EXPENSE - Per Company	2,718	
	Per Staff	903	(\$1,815)

To adjust to Company's actual expense per general ledger as the Company failed to substantiate its adjustments.

STAFF ADJUSTMENTS (Cont.)

(G) -	DEPRECIATION - Per Company	\$3,351	
	Per Staff	<u>1,092</u>	<u>(\$2,259)</u>

To adjust depreciation expense to Staff's calculation.

Pro Forma Annual Depreciation Expense:

Plant in Service	\$59,546
Less: Non Depreciable Plant	30,000
Fully Depreciated Plant	<u>0</u>
Depreciable Plant	\$29,546
Times: Staff Proposed Depreciation Rate	<u>5.00%</u>
Credit to Accumulated Depreciation	\$1,092
Less: Amort. of CIAC* @ 5.00%	<u>0</u>
Pro Forma Annual Depreciation Expense	<u>\$1,092</u>

RATE DESIGN

	Present	-Proposed Rates-	
	Rates	Company	Staff
<u>Monthly Usage Charge</u>			
5/8" x 3/4" Meter	\$ 18.00	\$ 45.00	\$ 30.00
3/4" Meter	18.00	45.00	45.00
1" Meter	N/A	N/A	75.00
1½" Meter	N/A	N/A	150.00
2" Meter	N/A	N/A	240.00
3" Meter	N/A	N/A	450.00
4" Meter	N/A	N/A	750.00
6" Meter	N/A	N/A	1,500.00
<u>Commodity Charge in Excess of Minimum</u>			
Gallons Included in Minimum	0	0	0
Flat Rate per 1,000 Gallons	\$ 2.50	\$ 6.50	N/A
Excess of Minimum - per 1,000 Gallons (0-3,000 Gallons)	N/A	N/A	\$ 2.90
Excess of Minimum - per 1,000 Gallons (3,001-15,000 Gallons)	N/A	N/A	\$ 4.00
Excess of Minimum - per 1,000 Gallons (Over 15,000 Gallons)	N/A	N/A	5.00
<u>Service Line and Meter Installation Charges</u>			
5/8" x 3/4" Meter	\$ 350.00	\$ 500.00	\$500.00
3/4" Meter	350.00	575.00	575.00
1" Meter	N/A	N/A	660.00
1½" Meter	N/A	N/A	900.00
2" Meter (compound)	N/A	N/A	1,525.00
3" Meter (compound)	N/A	N/A	2,165.00
4" Meter (compound)	N/A	N/A	3,360.00
6" Meter (turbo)	N/A	N/A	6,035.00
<u>Service Charges</u>			
Establishment	\$25.00	\$30.00	\$30.00
Establishment (After Hours)	25.00	45.00	45.00
Reconnection (Delinquent)	25.00	30.00	30.00
Reconnection (Delinquent) after hours	25.00	45.00	45.00
Meter Test (If Correct)	N/A	25.00	25.00
Deposit	*	*	*
Deposit Interest	*	3.00%	*
Re-Establishment (Within 12 Months)	**	**	**
NSF Check	10.00	15.00	15.00
Deferred Payment	N/A	N/A	1.50%
Meter Re-Read (If Correct)	5.00	10.00	10.00
Late Payment Penalty (per month)	N/A	5.0%	1.5%
Main Extension	N/A	N/A	Cost

* Per Commission Rules (R14-2-403.B)

** Months off system times the minimum (R14-2-403.D)

TYPICAL BILL ANALYSIS

General Service 5/8 X 3/4 - Inch Meter

Average Number of Customers: 31

<u>Company Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	3,686	\$27.21	\$68.96	\$41.75	153.4%
Median Usage	2,074	\$23.19	\$58.48	\$35.29	152.2%

<u>Staff Proposed</u>					
Average Usage	3,686	\$27.21	\$41.44	\$14.23	52.3%
Median Usage	2,074	\$23.19	\$36.01	\$12.82	55.3%

Present & Proposed Rates (Without Taxes)
General Service 5/8 X 3/4 - Inch Meter

<u>Gallons Consumption</u>	<u>Present Rates</u>	<u>Company Proposed Rates</u>	<u>% Increase</u>	<u>Staff Proposed Rates</u>	<u>% Increase</u>
0	\$18.00	\$45.00	150.0%	\$30.00	66.7%
1,000	20.50	51.50	151.2%	32.90	60.5%
2,000	23.00	58.00	152.2%	35.80	55.7%
3,000	25.50	64.50	152.9%	38.70	51.8%
4,000	28.00	71.00	153.6%	42.70	52.5%
5,000	30.50	77.50	154.1%	46.70	53.1%
6,000	33.00	84.00	154.5%	50.70	53.6%
7,000	35.50	90.50	154.9%	54.70	54.1%
8,000	38.00	97.00	155.3%	58.70	54.5%
9,000	40.50	103.50	155.6%	62.70	54.8%
10,000	43.00	110.00	155.8%	66.70	55.1%
15,000	55.50	142.50	156.8%	86.70	56.2%
20,000	68.00	175.00	157.4%	111.70	64.3%
25,000	80.50	207.50	157.8%	136.70	69.8%
50,000	143.00	370.00	158.7%	261.70	83.0%
75,000	205.50	532.50	159.1%	386.70	88.2%
100,000	268.00	695.00	159.3%	511.70	90.9%
125,000	330.50	857.50	159.5%	636.70	92.6%
150,000	393.00	1,020.00	159.5%	761.70	93.8%
175,000	455.50	1,182.50	159.6%	886.70	94.7%
200,000	518.00	1,345.00	159.7%	1,011.70	95.3%

SUMMARY OF FILING

	-- Present Rates --		-- Proposed Rates --	
	Company as Filed	Staff as Adjusted	Company as Filed	Staff as Adjusted
Revenues:				
Metered Water Revenue	\$6,989	\$6,989	\$21,655	\$10,582
Unmetered Water Revenue	0	0	0	0
Other Water Revenues	0	0	0	0
Total Operating Revenue	\$6,989	\$6,989	\$21,655	\$10,582
Operating Expenses:				
Operation and Maintenance	\$7,709	\$4,185	\$7,709	\$4,185
Depreciation	2,384	2,170	2,384	2,362
Property & Other Taxes	217	217	217	217
Income Tax	0	0	0	0
Total Operating Expense	\$10,310	\$6,572	\$10,310	\$6,764
Operating Income/(Loss)	(\$3,321)	\$417	\$11,345	\$3,818
Rate Base O.C.L.D.	\$45,325	\$33,505	\$45,325	\$33,505
Rate of Return - O.C.L.D.	-7.33%	1.24%	25.03%	11.40%
Times Interest Earned Ratio (Pre-Tax)*	N/A	N/A	N/A	N/A
Debt Service Coverage Ratio (Pre-Tax)*	N/A	N/A	N/A	N/A
Operating Margin	-47.52%	5.97%	52.39%	36.08%

* TIER and DSC ratios are reflected on Schedule DRR-1 which reflects the effect of the \$40,000 WIFA loan at 6 percent on the combined water and wastewater division totals.

RATE BASE

	----- Original Cost -----		
	Company	Adjustment	Staff
Plant in Service	\$106,290	(\$52,606) (A)	\$53,684
Less:			
Accum. Depreciation	61,709	(41,084) (B)	20,625
Net Plant	\$44,581	(\$11,522)	\$33,059
Less:			
Advances in Aid of Construction	\$0	\$0	\$0
Meter Deposits (Meter & Service Line)	0	0	0
Total Advances	\$0	\$0	\$0
Contributions Gross	\$0	\$0	\$0
Less:			
Amortization of CIAC	0	0	0
Net CIAC	\$0	\$0	\$0
Total Deductions	\$0	\$0	\$0
Plus:			
1/24 Power	\$0	\$0	\$0
1/8 Operation & Maint.	744	(298) (C)	446
Inventory	0	0	0
Prepayments	0	0	0
Total Additions	\$744	(\$298)	\$446
Rate Base	\$45,325	(\$11,820)	\$33,505

Explanation of Adjustment:

- A - See Schedule WW-2, page 2 of 3.
- B - See Schedule WW-2, page 3 of 3.
- C - Based on Staff adjustments to operating expenses.

PLANT ADJUSTMENT

	Company Exhibit	Adjustment	Staff Adjusted
301 Organization	\$0	\$0	\$0
302 Franchises	0	0	0
353 Land & Land Rights	30,000	(20,000)	10,000
354 Structures & Improvements	300	(300)	0
360 Wells & Springs	46,000	(36,695)	9,305
363 Services	2,040	(430)	1,610
368 Lift Station	0	0	0
370 Pump Station Receiving Wells	0	353	353
371 Effluent Pump	0	6,970	6,970
380 Treatment Plant	27,000	(1,554)	25,446
381 Plant Sewers	0	0	0
382 Effluent Lines	0	0	0
389 Other Plant Structure and Improvem	0	0	0
390 Office Furniture and Equipment	950	(950)	0
391 Transportation Equipment	0	0	0
393 Tools and Work Equipment	0	0	0
394 Laboratory Equipment	0	0	0
396 Communication Equipment	0	0	0
398 Other Tangible Plant	0	0	0
105 C.W.I.P.	0	0	0
TOTALS	\$106,290	(\$52,606) (A)	\$53,684

(A) Adjustments based on Staff Engineer's analysis.

ACCUMULATED DEPRECIATION ADJUSTMENT

	<u>Amount</u>
Accumulated Depreciation - Per Company	\$ 61,709
Accumulated Depreciation - Per Staff	20,625
Total Adjustment	\$ (41,084)

Explanation of Adjustment:

B - Accumulated depreciation balance per Staff Engineer, as of December 31, 2002	\$ 18,455
Plus: Depreciation expense 2003	<u>2,170</u>
Staff balance as of December 31, 2003	<u><u>20,625</u></u>

STATEMENT OF OPERATING INCOME

	Company Exhibit	Staff Adjustments	Staff Adjusted
Revenues:			
521 Flat Rate Revenues	\$6,989	\$0	\$6,989
474 Other Revenue	0	0	0
Total Operating Revenue	\$6,989	\$0	\$6,989
Operating Expenses:			
701 Salaries and Wages	\$0	\$0	\$0
710 Purchased Wastewater Treatment	0	0	0
711 Sludge Removal	0	0	0
715 Purchased Power	296	0	296
716 Fuel for Power Production	0	0	0
718 Chemicals	0	0	0
720 Repairs and Maintenance	367	(23) (A)	344
721 Office Supplies	0	501 (B)	501
731 Contractual Services Profesional	953	1,202 (C)	2,155
735 Contractual Services Testing	1,069	(1,069) (D)	0
736 Contractual Services Other	3,061	(3,061) (E)	0
740 Rent	150	(150) (F)	0
750 Transportation Expense	53	0	53
755 Insurance General Liability	0	0	0
765 Rate Case Expense	1,000	(650) (G)	350
775 Miscellaneous Expense	760	(274) (H)	486
403 Depreciation Expense	2,384	(214) (I)	2,170
408.11 Property Taxes	217	0	217
409 Income Tax	0	0	0
Total Operating Expenses	\$10,310	(\$3,738)	\$6,572

OPERATING INCOME/(LOSS)	(\$3,321)	\$3,738	\$417
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Other Income/(Expense):

419 Interest and Dividend Income	\$0	\$0	\$0
421 Non-Utility Income	0	0	0
427 Interest Expense	0	8 (J)	8
426 Miscellaneous Non-Utility Expense	0	0	0

Total Other Income/(Expense)	\$0	(\$8)	(\$8)
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NET INCOME/(LOSS)	(\$3,321)	\$3,730	\$409
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STAFF ADJUSTMENTS

(A)	REPAIRS AND MAINTENANCE - Per Company Per Staff	\$367 344	<u>(\$23)</u>
	To correct Company's 10-year average, Staff removed highest and lowest years, and used the truncated average of 8 years. Staff allocated 35% of the eight-year average expense to the wastewater division and 65% to the water division.		
(B)	OFFICE SUPPLIES - Per Company Per Staff	0 501	<u>\$501</u>
	To record 35% allocation from water division expense.		
(C)	CONTRACTUAL SERVICES PROFESSIONAL - Per Company Per Staff	953 2,155	<u>\$1,202</u>
	To record 35% of actual expense.		
(D)	CONTRACTUAL SERVICES TESTING - per Company Per Staff	\$1,069 0	<u>(\$1,069)</u>
	To remove testing fee submitted by the Company. Community septic tank, general permit required - no fee.		
(E)	CONTRACTUAL SERVICES OTHER - per Company Per Staff	3,061 0	<u>(\$3,061)</u>
	Community septic tank, minimum maintenance required. See adjustment (C). Actual expense recorded.		
(F)	RENT EXPENSE - per Company Per Staff	\$150 0	<u>(\$150)</u>
	To remove unsubstantiated entry.		

STAFF ADJUSTMENTS (Cont.)

(G)	RATE CASE EXPENSE - Per Company	217	
	Per Staff	217	\$0

35% allocation of the rate case expense to the Wastewater Company.

(H)	MISCELLANEOUS EXPENSE - Per Company	0	
	Per Staff	0	\$0

To record 35% of actual expense.

(I)	DEPRECIATION - Per Company	\$0	
	Per Staff	0	\$0

To adjust depreciation expense to Staff's calculation.

Pro Forma Annual Depreciation Expense:

Plant in Service	\$53,684
Less: Non Depreciable Plant	10,000
Fully Depreciated Plant	0
Depreciable Plant	\$43,684
Times: Staff Proposed Depreciation Rate	0.00%
Credit to Accumulated Depreciation	\$3
Less: Amort. of CIAC* @ 0.00%	0
Pro Forma Annual Depreciation Expense	\$3

(J)	INTEREST EXPENSE - Per Company	0	
	Per Staff	(8)	(\$8)

To record 35% of interest expense.

Oak Creek Utility Corp - Wastewater
Docket No. WS-02061A-04-0835
Test Year Ended December 31, 2003

Schedule WW-4

RATE DESIGN

		Present	-Proposed Rates-	
		Rates	Company	Staff
<u>Monthly Usage Charge</u>				
<u>Measured Rate Customers</u>				
Residential	(monthly minimum charge)	\$ 15.00	\$ 45.00	\$ 20.00
Commercial	(monthly minimum charge)	\$ 45.00	\$ 45.00	\$ 55.00
<u>Measured Rate Customers</u>				
Residential	(per 1,000 gallons of usage)	\$ 1.00	\$ 3.50	\$ 2.25
Commercial	(per 1,000 gallons of usage)	\$ 3.50	\$ 3.50	\$ 4.00
<u>Service Lateral Installation Charges</u>				
	Residential	\$ 350.00	\$ 500.00	\$ 500.00
	Commercial	\$ 350.00	\$ 575.00	\$ 575.00
<u>Service Charges</u>				
	Establishment	\$25.00	\$30.00	\$30.00
	Establishment (After Hours)	25.00	45.00	45.00
	Reconnection (Delinquent)	25.00	30.00	30.00
	Deposit	*	*	*
	Deposit Interest	*	3.00%	*
	Re-Establishment (Within 12 Months)	**	**	**
	NSF Check	10.00	15.00	15.00

* Per Commission Rules (R14-2-403.B)

** Months off system times the minimum (R14-2-403.D)

TYPICAL BILL ANALYSIS

Wastewater

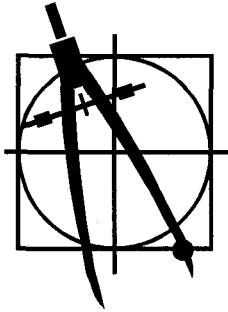
Average Number of Customers: 31

<u>Company Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	3,686	\$18.69	\$57.90	\$39.21	209.8%
Median Usage	2,074	\$17.07	\$52.26	\$35.19	206.2%

<u>Staff Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	3,686	\$18.69	\$28.29	\$9.60	51.4%
Median Usage	2,074	\$17.07	\$24.67	\$7.60	44.5%

Present & Proposed Rates (Without Taxes) Wastewater

<u>Gallons Consumption</u>	<u>Present Rates</u>	<u>Company Proposed Rates</u>	<u>% Increase</u>	<u>Staff Proposed Rates</u>	<u>% Increase</u>
0	\$15.00	\$45.00	200.0%	\$20.00	33.3%
1,000	16.00	48.50	203.1%	22.25	39.1%
2,000	17.00	52.00	205.9%	24.50	44.1%
3,000	18.00	55.50	208.3%	26.75	48.6%
4,000	19.00	59.00	210.5%	29.00	52.6%
5,000	20.00	62.50	212.5%	31.25	56.3%
6,000	21.00	66.00	214.3%	33.50	59.5%
7,000	22.00	69.50	215.9%	35.75	62.5%
8,000	23.00	73.00	217.4%	38.00	65.2%
9,000	24.00	76.50	218.8%	40.25	67.7%
10,000	25.00	80.00	220.0%	42.50	70.0%
15,000	30.00	97.50	225.0%	53.75	79.2%
20,000	35.00	115.00	228.6%	65.00	85.7%
25,000	40.00	132.50	231.3%	76.25	90.6%
50,000	65.00	220.00	238.5%	132.50	103.8%
75,000	90.00	307.50	241.7%	188.75	109.7%
100,000	115.00	395.00	243.5%	245.00	113.0%
125,000	140.00	482.50	244.6%	301.25	115.2%
150,000	165.00	570.00	245.5%	357.50	116.7%
175,000	190.00	657.50	246.1%	413.75	117.8%
200,000	215.00	745.00	246.5%	470.00	118.6%



**Engineering Report
For
OAK CREEK
Utility Corporation
Docket No. WS-02061A-04-0835
(Rates)
Docket No. WS-02061A-04-0836
(Financing)**

RECOMMENDATIONS

- I. The Arizona Department of Environmental Quality ("DEQ") reported that Oak Creek Utility Corporation is delivering water which meets the standards required by the Arizona Administrative Code, Title 18 Chapter 4.
- II. DEQ did identify the lack of a microbiological site sampling plan. The lack of a site sampling represents a public health risk.

Therefore Staff recommends that any permanent rates and charges in this matter shall become effective on the first day of the month after the Director of the Utilities Division receives notice from the Arizona Department of Environmental Quality that Oak Creek Utility Corporation has an approved microbiological site sampling plan. (See §D of this report for discussion and details about the DEQ compliance deficiencies.)

- III. Staff recommends that the Company amend its proposed curtailment tariff and file that amended curtailment tariff within 45 days after the effective date of any decision and order pursuant to this application. That amended curtailment shall contain the following provision:

"If a customer believes he/she has been disconnected in error, the customer may contact the Commission's Consumer Services Section at 1-800-222-7000 to initiate an investigation."

Staff further recommends that the proposed order in this matter shall contain the following two directives to the Company:

1. Oak Creek Utility Corporation shall notify its customers of this new curtailment tariff as part of its next regularly scheduled billing after the effective of the curtailment tariff but no later than sixty (60) days after the effective date of the tariff, and
2. Oak Creek Utility Corporation shall provide a copy of the curtailment tariff to any customer, upon request.

- III. Staff recommends that Oak Creek Utility Corporation adopt the specific depreciation rates by NARUC category found in Exhibits 3A and 3B of this report. (See §K for a discussion of the recommended rates.)
- IV. From a technical basis, Staff recommends financing approval of the storage tank construction project, including booster pumps, controls, fencing and well metering. This recommendation is limited to the engineering aspects of the application and makes no judgment concerning the financial fitness of the Company to service this loan nor does it imply a future treatment for rate making purposes.

Staff further recommends that the storage tank project shall be completed within 18 months after the effective date of any decision and order pursuant to this application. The Company shall notify the Director of the Utilities Division when the project is completed.

Staff further recommends that the existing well meter shall be relocated, or as an alternative, a new well meter shall be installed between the well discharge and the storage tank, or in such a location to best conform to the manufacturer's recommended location and manufacturer's recommended function. (See §E and §I for further discussion.)

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EXHIBITS

CERTIFICATED AREA AND LOCATION OF COMPANY	EXHIBIT 1
PROCESS SCHEMATIC	EXHIBIT 2
DEPRECIATION RATES.....	EXHIBITS 3A & B
PLANT IN SERVICE.....	EXHIBITS 4A & B

APPENDIX

WORK PAPERS

A. LOCATION OF COMPANY

Oak Creek Utility Corporation (herein also "Company" or "Oak Creek Utility"), provides water and sewer service to a small 45 lot subdivision on the east side of Oak Creek, near the old "Indian Gardens" and "sand statues" area, along Highway 89A. The subdivision was originally platted in 1966. Oak Creek Utility presently serves about 30 customers within a 6.63 acre certificated area. **Exhibit 1** describes the location and certificated area of the water company within Coconino County.

B. PLANT IN SERVICE

The plant facilities were visited on May 25, 2004, by Lyndon Hammon in the accompaniment of Mr. Randy Sosin, who is the president of SOS Water And Wastewater Treatment, Inc., and the contractual on-site operator of the water and wastewater systems.

The water system consists of a well which directly pressurizes a hydro-pneumatic tank and distribution mains. The sewage system consists of a collection system which drains to a small pumping station. The sewage is then pumped to a community septic tank and leach field.

The water system has adequate well production but provides no storage. Arizona Department of Environmental Quality ("DEQ") rules require one day's storage and the company has been given notice from DEQ of this rule violation. This situation is discussed further in this report under §E. Financing. **Exhibit 2** provides process schematics for the existing water and wastewater systems.

Facility Summary

	Water System	Sewage System
ADWR ID No.	55-802265	
Casing Size	8 inch	
Casing Depth	450 ft	
Pump Type	Submersible	
Pump Size	5 Hp	
Pump Yield	50 gal/min	
Well Meter	yes, 2 inches	
Storage	<i>None</i> <i>10,000 gal is</i> <i>proposed</i>	10,000 Gallon septic tank and leach field
Booster Pumps	<i>None</i> <i>Two 3.5 Hp pumps are</i> <i>proposed</i>	Two 10 Hp lift pumps 72 gal/min
Pressure Tanks	2,000 gal	

	Water	Sewer
Distribution/ Collection Mains		
Size	4 inch	8 inch
Quantity	2,560 lineal feet	2230
Material	Asbestos Cement	Vitrified Clay
Meters	29 individual meters, 5/8 x 3/4 inch galvanized steel service lines	

The last rate review and adjustment for Oak Creek Utility was made in 1984. The new owner, Mr. Dean Orem, has been working hard to organize the financial records, going forward, but the past records are not as complete as Staff would prefer. Therefore, for purposes of this instant rate application, Staff attempted to reconstruct the present rate base, based upon interviews with the operator, a site inspection, and the use of standard water industry cost estimating methods. Original costs and reproduction costs are reported in **Exhibits 4A and 4B**. (Reproduction costs represent the cost to build a new system with equivalent performance and quality.) The final rate making treatment of these plant in service costs is contained in the overall accounting and financial staff report.

C. ARSENIC

The U.S. Environmental Protection Agency (EPA) has reduced the arsenic maximum contaminant level (MCL) in drinking water from 50 micrograms per liter ($\mu\text{g/l}$) to 10 $\mu\text{g/l}$. The date for compliance with the new MCL is January 23rd, 2006.

The most recent lab analyses from DEQ indicate that the arsenic level in the single well is 8.7 $\mu\text{g/l}$. Based on this sample data, the Company is in compliance with the new arsenic MCL.

D. ARIZONA DEPARTMENT OF ENVIRONMENTAL QUALITY COMPLIANCE (DEQ)

Water

The Arizona Department of Environmental Quality ("DEQ") reported that Oak Creek Utility Corporation is delivering water which meets the standards required by the Arizona Administrative Code, Title 18 Chapter 4.

Although no water quality problems were reported, DEQ did identify two major operation and maintenance deficiencies. Those deficiencies were the lack of a one day's minimum storage and the lack of an approved Microbiological Site Sampling Plan. A microbiological site sampling plan is required by State rule and is intended to insure that the procedure,

quantity, and location of coliform sampling will truly represent the biological quality within a water distribution system. Because of this potential public health risk, Staff recommends that the Company submit evidence of a DEQ approved microbiological site sampling plan before the new rates become effective in this case.

In a subsequent docket, the Company has applied for financing approval for the construction of a new storage tank and ancillary equipment, which will bring it in compliance with the DEQ storage rule.

In summary, Staff recommends that any permanent rates and charges in this matter shall become effective on the first day of the month after the Director of the Utilities Division receives notice from the Arizona Department of Environmental Quality that Oak Creek Utility Corporation has an approved microbiological site sampling plan.

Wastewater

The wastewater system consists of a simple septic tank and subsurface disposal system for the effluent. Under DEQ permit rules, septic tank systems of certain sizes and disposal densities are treated differently from more sophisticated bio-mechanical systems. The Company filed, with DEQ, a "Notice of Disposal" which qualifies them for a general permit. DEQ confirmed that the facility has a General Permit in good standing in accordance with its aquifer protection rules, and that no monitoring or reporting is required at this time.

E. FINANCING.

Arizona Department of Environmental Quality Rule R18-5-503A states:

"The minimum storage capacity for a CWS or a noncommunity water system that serves a residential population or a school shall be equal to the average daily demand during the peak month of the year."

("CWS" means a community water system. Since Oak Creek Utility has more than 15 year-round service connections, it is a community water system.)

As it stands, Oak Creek Utility Corporation has a single well and provides no storage. DEQ has cited the Company for this rule violation. In order to comply with the DEQ storage requirement, Oak Creek Utility has applied in Docket No. WS-02061A-04-0836 for financing approval to construct a 10,000 gallon storage tank, two 3.5 horsepower booster pumps, controls, and fencing. The Company anticipates borrowing \$40,000 from the Water Infrastructure Finance Authority to meet the capital needs of the project. The storage tank will meet the present and future needs and the cost seems reasonable. From a technical basis, Staff recommends financing approval of the construction project. This recommendation is limited to the engineering facets of the application and makes no judgment concerning the

financial fitness of the Company to service this loan nor does it imply a future treatment for rate making purposes.

Staff further recommends that the storage tank project shall be completed within 18 months after the effective date of any decision and order pursuant to this application. The Company shall notify the Director of the Utilities Division when the project is completed.

Staff further recommends that the existing well meter shall be relocated, or as an alternative, a new well meter shall be installed between the well discharge and the storage tank, or in such a location to best conform to the manufacturer's recommended location and manufacturer's recommended function. (For additional discussion, refer to the "Non-Account Water" portion of §I of this report.)

F. ARIZONA CORPORATION COMMISSION COMPLIANCE

A check with the Utilities Division Compliance Unit showed no outstanding compliance issues.

G. ARIZONA DEPARTMENT OF WATER RESOURCES COMPLIANCE

Oak Creek Utility Corporation is not within any Active Management Area and is not subject to any monitoring and reporting requirements for groundwater withdrawals.

H. WATER TESTING EXPENSE

On December 8, 1998, DEQ adopted rules which provide for a monitoring assistance program (MAP). The MAP program was fully implemented in 1999. On October 16, 2001, rule amendments were promulgated which changed the fee structure and some sampling protocol. Starting January 1, 2002, water companies began paying a fixed \$250 per year fee, plus an additional fee of \$2.57 per service connection, regardless of meter size for participation in the MAP program. Participation in the MAP program is mandatory for water systems which serve less than 10,000 persons, (approximately 3,300 service connections), and Oak Creek Utility is subject to the MAP program.

Water testing costs were calculated, based on the following assumptions:

- MAP will do baseline testing on all parameters except copper, lead, nitrates, and coliform bacteria.
- DEQ testing is performed in 3 year compliance cycles. Therefore, monitoring costs are estimated for a 3 year compliance period and then presented as a *pro forma* expense on an annualized basis.

- Expenses are included for a complete inorganic analyses at each well. This will provide important aesthetic and water quality information for the Company and the consumer (i.e., hardness, salinity, iron, manganese, alkalinity).
- All monitoring expenses are based on Staff's best knowledge of lab costs and methodology and one point of entry for each water system.
- The estimated water testing expenses represent a minimum cost based on no "hits", and assumes the Company has qualified for reduced lead and copper sampling. If any constituents were found, then the testing costs would dramatically increase.

Water testing expenses should be adjusted to the annual expense amount shown in the table below.

Water Testing Cost

Monitoring – 1 well (Tests per 3 years, unless noted.)	Cost per test	No. of tests per 3 years	Total 3 year cost	Annual Cost
Bacteriological – monthly	\$ 20	36	720	240
Inorganics (& secondary)	\$240	1	240	80
Nitrates – annual	\$ 25	3	75	25
Lead & Copper – annual	\$ 25	5	125	42
MAP fees (based on 29 services at end of TY)				\$325
Total				\$ 712

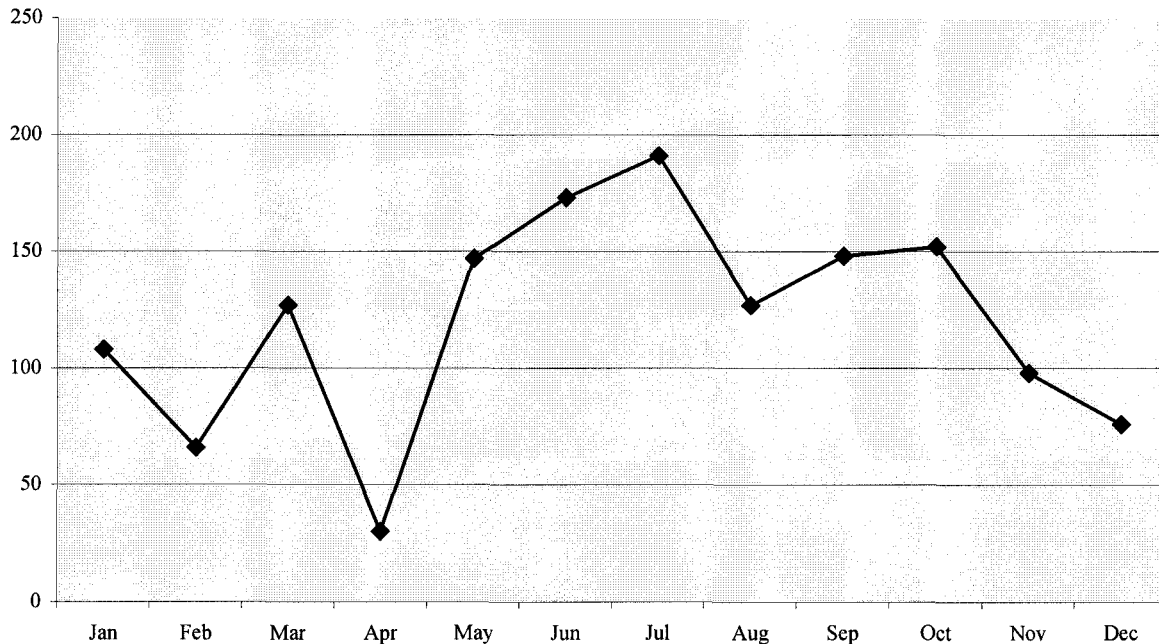
There is no required monitoring, testing, or reporting of the septic tank effluent.

I. WATER USE

Water Sold

Based on the information provided by the Company, water use for the year 2003 is presented below. For Oak Creek Utility, the high monthly domestic water use was 190 gal/day-service in June, and the low monthly domestic water use was 30 gal/day-service in April. (The average during peak month, or 190 gal/day-service times 30 services equals about 6,000 gallons. This is within the 10,000 gallon storage capacity proposed and meets the DEQ standard.) The average annual use was 120 gal/day-service. Monthly water use during the test year is shown in the figure below:

Oak Creek Utility Corporation
Water Use (gal/day-service)



Non-account Water

Non-account water should be 10% or less and never more than 15%. It is important to be able to reconcile the difference between water sold and the water produced by the source. A water balance will allow a water company to identify water and revenue losses due to leakage, theft, and flushing. Unfortunately, the monthly non-account water was ambiguous and varied from a 77% loss to a 133% gain.

One possible explanation may involve the location of the well meter. A totalizing turbine well meter usually works best in an application where the flows are relatively constant. In other words, the well pump turns on and pumps at a fairly constant rate through the turbine meter, and then turns off. At Oak Creek, the well meter is located on the demand side of the pressure tank. Flows vary according to the water system demand and can fluctuate from zero to a maximum system demand. Under this condition, a turbine meter would typically read low at low flows. This would result in a situation where water pumped would be less than water sold, which is the exact circumstance in this case.

The storage tank project offers in ideal time to fix the metering problem since the well piping will be reconfigured during the storage tank construction. Therefore Staff recommends that the existing well meter shall be relocated, or as an alternative, a new well meter shall be installed between the well discharge and the storage tank, or in such a location to best conform to the manufacturer's recommended location and manufacturer's recommended function.

J. GROWTH

Oak Creek Utility has historically averaged growth at about one service connection every two years. There is no reason to expect a dramatic change and this rate would be a reasonable prediction for the Company's growth. The subdivision was originally platted as a mobile home subdivision of 45 lots. The small lot size and topography will likely dictate some combining of existing lots for future development and therefore the ultimate customer base will probably be limited to 40 lots or less.

K. DEPRECIATION RATES

In recent orders, the Commission has been shifting away from the use of composite rates in favor of individual depreciation rates by NARUC category. (NARUC is an acronym for National Association of Regulatory Utility Commissioners.)

Staff has developed typical and customary depreciation rates within a range of anticipated equipment life. These rates are presented in **Exhibits 3A and 3B**, and were used to recalculate the annual depreciation expense and accumulated depreciation expense for the Company in Exhibits 4A and 4B, "Plant In Service". It is recommended that the Company use depreciation rates by individual NARUC category, as delineated in Exhibits 3A and 3B.

L. CURTAILMENT TARIFF

A curtailment tariff is an effective tool to allow a water company to manage its resources during periods of shortages due to pump breakdowns, droughts, or other unforeseeable events. Oak Creek Utility Corporation does not have a curtailment tariff, but has wisely chosen this rate application process to prepare and file such a tariff. The proposed curtailment tariff closely follows recommended language and conditions, with a minor exception, which involves customer notification of the right for a review by the Commission's Consumer Services Section. Therefore, Staff recommends that the Company file an amended curtailment tariff within 45 days after the effective date of any decision and order pursuant to this application and that amended curtailment shall contain the following provision:

“If a customer believes he/she has been disconnected in error, the customer may contact the Commission’s Consumer Services Section at 1-800-222-7000 to initiate an investigation.

Staff also recommends that the proposed order in this matter shall contain the following two directives to the Company:

1. Oak Creek Utility Corporation shall notify its customers of this new curtailment tariff as part of its next regularly scheduled billing after the effective of the curtailment tariff but no later than sixty (60) days after the effective date of the tariff, and
2. Oak Creek Utility Corporation shall provide a copy of the curtailment tariff to any customer, upon request.

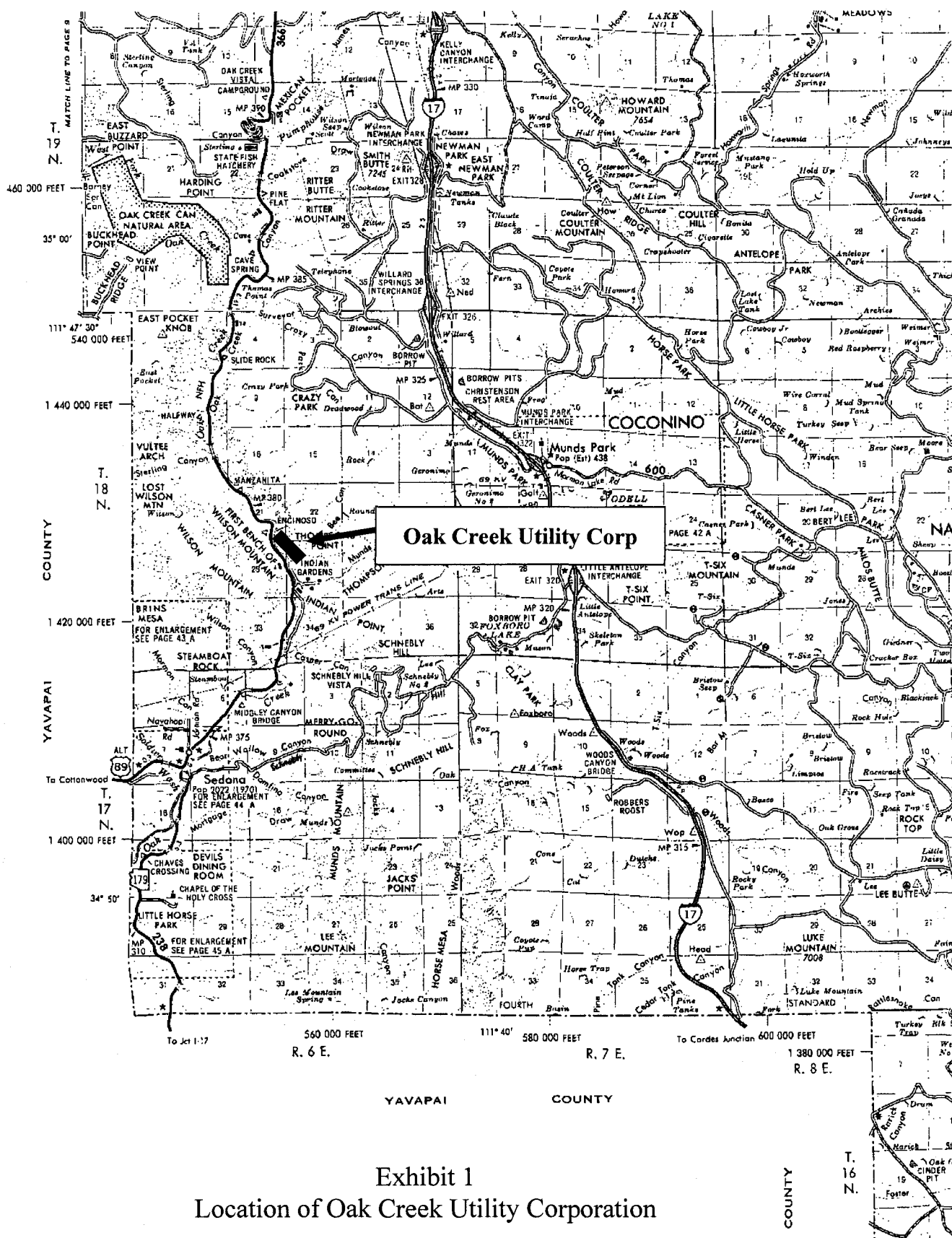


Exhibit 1
Location of Oak Creek Utility Corporation

Oak Creek Utility Corporation

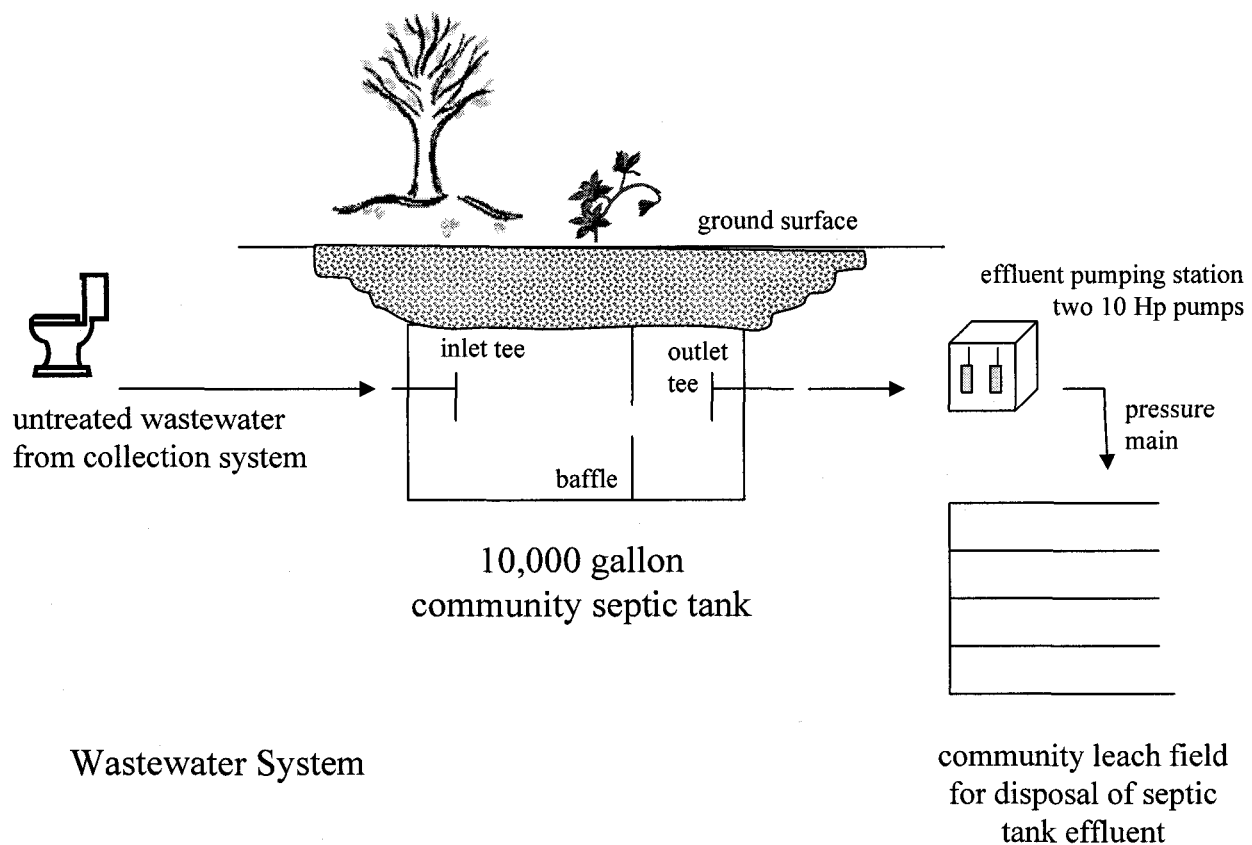
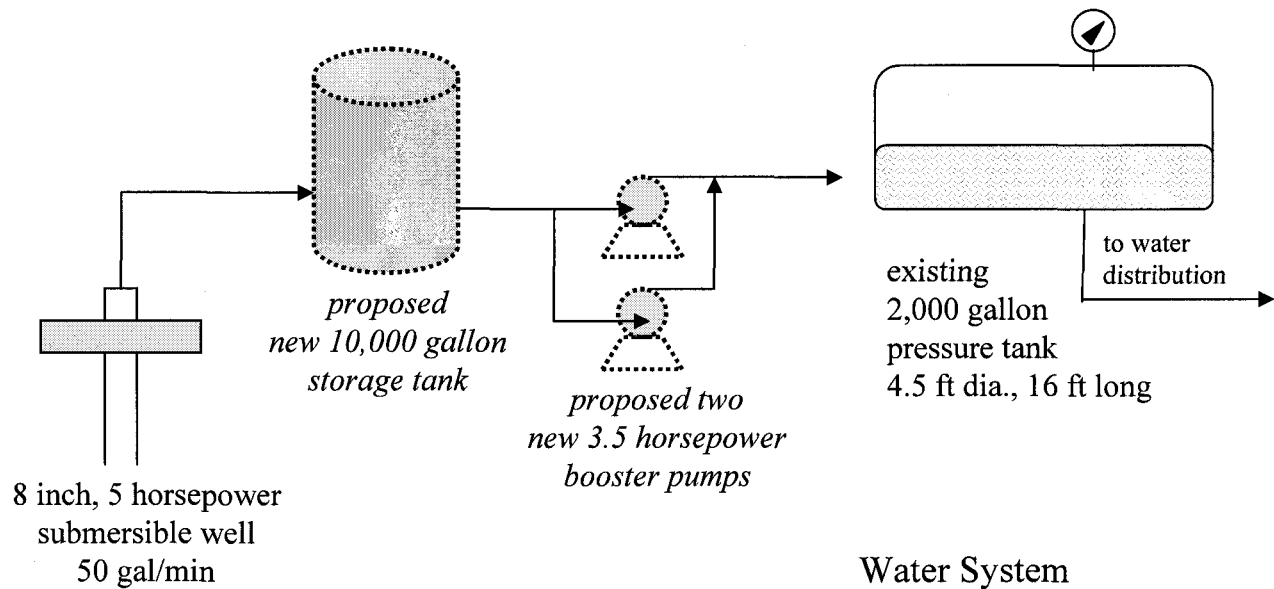


Exhibit 2

EXHIBIT 3 A

TYPICAL DEPRECIATION RATES FOR WATER COMPANIES

NARUC Account No.	Depreciable Plant	Average Service Life (Years)	Annual Accrual Rate (%)
304	Structures & Improvements	30	3.33
305	Collecting & Impounding Reservoirs	40	2.50
306	Lake, River, Canal Intakes	40	2.50
307	Wells & Springs	30	3.33
308	Infiltration Galleries	15	6.67
309	Raw Water Supply Mains	50	2.00
310	Power Generation Equipment	20	5.00
311	Pumping Equipment	8	12.5
320	Water Treatment Equipment		
320.1	Water Treatment Plants	30	3.33
320.2	Solution Chemical Feeders	5	20.0
330	Distribution Reservoirs & Standpipes		
330.1	Storage Tanks	45	2.22
330.2	Pressure Tanks	20	5.00
331	Transmission & Distribution Mains	50	2.00
333	Services	30	3.33
334	Meters	12	8.33
335	Hydrants	50	2.00
336	Backflow Prevention Devices	15	6.67
339	Other Plant & Misc Equipment	15	6.67
340	Office Furniture & Equipment	15	6.67
340.1	Computers & Software	5	20.00
341	Transportation Equipment	5	20.00
342	Stores Equipment	25	4.00
343	Tools, Shop & Garage Equipment	20	5.00
344	Laboratory Equipment	10	10.00
345	Power Operated Equipment	20	5.00
346	Communication Equipment	10	10.00
347	Miscellaneous Equipment	10	10.00
348	Other Tangible Plant	----	----

NOTES:

1. These depreciation rates represent average expected rates. Water companies may experience different rates due to variations in construction, environment, or the physical and chemical characteristics of the water.
2. Acct. 348, Other Tangible Plant may vary from 5% to 50%. The depreciation rate would be set in accordance with the specific capital items in this account.

EXHIBIT 3 B

TYPICAL DEPRECIATION RATES FOR WASTEWATER UTILITIES

NARUC Acct. No.	Depreciable Plant	Average Service Life (Years)	Annual Accrual Rate (%)
354	Structures & Improvements	30	3.33
355	Power Generation Equipment	20	5.00
360	Collection Sewers – Force	50	2.0
361	Collection Sewers- Gravity	50	2.0
362	Special Collecting Structures	50	2.0
363	Services to Customers	50	2.0
364	Flow Measuring Devices	10	10.0
365	Flow Measuring Installations	10	10.00
366	Reuse Services	50	2.00
367	Reuse Meters & Meter Installations	12	8.33
370	Receiving Wells	30	3.33
371	Pumping Equipment	8	12.50
374	Reuse Distribution Reservoirs	40	2.50
375	Reuse Transmission & Distribution System	40	2.50
380	Treatment & Disposal Equipment	20	5.0
381	Plant Sewers	20	5.0
382	Outfall Sewer Lines	30	3.33
389	Other Plant & Miscellaneous Equipment	15	6.67
390	Office Furniture & Equipment	15	6.67
390.1	Computers & Software	5	20.0
391	Transportation Equipment	5	20.0
392	Stores Equipment	25	4.0
393	Tools, Shop & Garage Equipment	20	5.0
394	Laboratory Equipment	10	10.0
395	Power Operated Equipment	20	5.0
396	Communication Equipment	10	10.0
397	Miscellaneous Equipment	10	10.0
398	Other Tangible Plant	----	----

NOTES:

1. These depreciation rates represent average expected rates. Wastewater companies may experience different rates due to variations in construction, environment, or the physical and chemical characteristics of the water.
2. Acct. 398, Other Tangible Plant may vary from 5% to 50%. The depreciation rate would be set in accordance with the specific capital items in this account.

EXHIBIT 4 A
PLANT IN SERVICE STUDY

SEWER	original cost	years in service	service life	annual depreciation	accumulated depreciation	OCLD	reproduction cost (2003\$)	annual depreciation at flat 5%
353 land and land rights	\$10,000			0	0	\$10,000	\$10,000	
354 structures and improvements								
360 & 361 collection mains, gravity & pressure 2230 feet @ 11.20 /ft (2003\$) installed 1966	\$5,650	37	50	\$113	\$4,181	\$1,469	\$24,976	\$283
14 manholes @ \$855 (2003\$) installed 1966	\$2,120	37	50	\$42	\$1,569	\$551	\$11,970	\$106
3 cleanouts @ \$160 (1995\$) installed 1966	\$105	37	50	\$2	\$78	\$27	\$480	\$5
sewer line mod/pump access 1995	\$1,430	8	50	\$29	\$229	\$1,201	\$1,835	\$72
363 service laterals								
46 laterals @ \$ 100 (1995\$) installed 1966	\$1,610	37	50	\$32	\$1,191	\$419	\$5,454	\$81
370 pump station receiving wells \$ 1997 (2003\$) installed 1966	\$353	37	30	\$0	\$353	\$0	\$1,997	\$18
371 mechanical pumping equipment two 10 Hp pumps, controls installed 1998	\$6,980	5	8	\$873	\$4,363	\$2,618	\$7,680	\$349
380 treatment plant								
septic tank installed 1966	\$2,555	37	20	\$0	\$2,555	\$0	\$14,430	\$128
outfall to field installed 1966	\$2,030	37	20	\$0	\$2,030	\$0	\$9,275	\$102
distribution box installed 1966	\$270	37	20	\$0	\$270	\$0	\$1,524	\$14
leach field installed 2002	\$18,537	1	20	\$927	\$927	\$17,610	\$19,327	\$927
alarms installed 1999	\$624	4	12	\$52	\$208	\$416	\$430	\$31
effluent line & access modifications 1995	\$1,430	7	20	\$72	\$501	\$930	\$1,710	\$72
TOTAL (excluding land)	\$43,694			\$2,141	\$18,454	\$25,240	\$101,088	\$2,185
TOTAL (including land)	\$53,694			\$2,141	\$18,454	\$35,240	\$111,088	
Composite Depreciation Rate	\$2,141	=		4.90%				
annual depreciation expense/ total plant in service as original cost, excluding land	\$43,694							

EXHIBIT 4 B
PLANT IN SERVICE STUDY

WATER	orig cost	years in service	service life	annual depreciation	accumulated depreciation	OCLD	reproduction cost (2003\$)	annual depreciation at flat 5%
land and land rights	\$30,000			\$0	\$0	\$30,000	\$30,000	
304 structures and improvements fence installed 1998	\$866	5	30	\$29	\$144	\$722	\$890	\$43
307 wells and springs drill and case installed 1966	\$3,985	37	30	\$0	\$3,985	\$0	\$22,500	\$199
311 pumping equipment well pump installed 1998	\$3,630	5	8	\$454	\$2,269	\$1,361	\$4,000	\$182
330 pressure tanks 2000 gal pressure tank installed 1988	\$3,485	16	20	\$174	\$2,788	\$697	\$4,460	\$174
331 distribution mains 2560 4 inch ACP	\$10,550	37	50	\$211	\$7,807	\$2,743	\$40,960	\$528
333 services 46 service lines installed 1966	\$3,725	37	30	\$0	\$3,725	\$0	\$17,250	\$186
334 meters well meter 2 inch - installed 1999	\$165	3	12	\$14	\$41	\$124	\$173	\$8
house connection	\$1,700	37	12	\$0	\$1,700	\$0	\$3,480	\$85
house connection instld 1995	\$1,440	8	12	\$120	\$960	\$480	\$1,585	\$72
TOTAL (excluding land)	\$29,546			\$1,002	\$23,419	\$6,127	\$95,298	\$1,477
TOTAL (including land)	\$59,546			\$1,002	\$23,419	\$36,127	\$125,298	
Composite Depreciation Rate =	\$1,002	=	3.39%					
annual depreciation expense/ total plant in service as original cost, excluding land	\$29,546	185	204.0339	\$1,002	\$23,419	\$36,127	\$125,298	\$1,477

APPENDIX
WORK PAPERS

WORK PAPERS

Sewer

Approved land costs were used from order in previous rate case in 1984 = \$10,000

Laterals

$(100) \times (78/291) \text{ cost index} = \text{about } 35\$ \times 46 = 1610 \text{ (1966\$)}$

Collection mains

8 inch is \$11.20/ft (2003\$) Means* $\times 2230 \text{ ft} \times (78/345) \text{ cost index} = 5650 \text{ (1966\$)}$

As a comparable cost, saddlebrooke average manhole cost was 832 (1995\$).

Means* estimate is 855 (2003\$). Use Means in this calculation.

$(855) \times 14 \times (65/367) \text{ cost index} = 2120 \text{ (1966\$)}$

saddlebrooke average cleanout cost = 160 (1995\$)

$(160) \times 3 \times (65/296) \text{ cost index} = 105 \text{ (1966\$)}$

Pump station – structure

Assume cost is for four ft dia precast manhole. Plans show 10 ft deep. Use Means*

manhole	1475
depth	197
slab top	<u>325</u>
total	$1997 \text{ (2003\$)} \times (65/367) \text{ index} = 353 \text{ (1966\$)}$

Mechanical pumping equipment

two 10 Hp sewage pumps	= 5,000 (2001\$) (Richardson**)
controls (600 each)	= 1,200 (2001\$)
labor 24 hr each @ 30\$/hr	= 1,440 (2001\$)
total	= 7,640 (2001\$)

Assume 5 years old, and 8 year life, therefore installed in 1998.

Original cost = $(7640) \times (485/531) \text{ cost index} = 6980 \text{ (1998\$)}$

Treatment plant

Septic tank 10,000 gal $(10 \text{ ft} \times 30 \text{ ft} \times 8 \text{ ft}) = 12000 \text{ (2003\$)} \text{ Means} \times (65/367) = 2125 \text{ (1966\$)}$

Excavation = $9\$/\text{yd}^3 \times (270 \text{ yd}^3) = 2430 \text{ (2003\$)} \times (65/367) = 430 \text{ (1966\$)}$

Note

* "RSMeans Building Construction Data 2003"

** "Richardson Process Plant Construction Estimating Standards 2001"

Distribution box 1: (materials + excavation) = 90 (1966\$) from Means
Box 2 is twice as large. Costs are proportional to size. Therefore cost = 180 (1966\$)

Outfall to field about 350 feet 3 inch steel. 26.50/ft (2003\$)
Cost = $26.50 \times 350 \times (69/315)$ index = 2030 (1966\$)

Leach Field
 $11881 + 6656 = 18537$ (2002\$) $\times 367/352$ cost index = \$19,327 (2002\$)

For reproduction cost new: land, franchises, and intangibles are not trended.

WATER

Approved land costs from previous rate case 1984 = \$30,000

Well: assume cost of drilling and casing = 50\$/ft (2003\$)
Cost = $450 \text{ ft} \times 50\$/\text{ft} \times (65/367)$ index = 3985 (1966\$)

Well pump – means list 3400 (2003\$) for 5 HP submersible pump
Well controls – estimate 600 (2003\$) = index = $485/534 = 3630$ (1998\$)


Pressure tank – assume in service 1988
 $2270 \text{ tank} + 615 \text{ coating} + 600 \text{ controls} = 3485$ (1988\$) $\times (275/215) = 4460$ (2003\$)

Water main cost – from actual Arizona data 4 inch is 16\$/ft (2001\$)
Cost = $16 \times 2560 = 40960$ (2001\$) $\times (86/334)$ index = 10550 (1966\$)

46 service lines @ 375 each = 17250 (2003\$) $\times (68/315) = 3724$
29 meters @ 120 = 3480 (2003\$) $\times (101/207) = 1698$ (1966\$)

**EXHIBIT A
MEMORANDUM**

TO: Elena Zestrijan
Public Utilities Analyst III
Financial and Regulatory Analysis Section, Utilities Division

FROM: D. R. Rogers 
Public Utilities Analyst IV
Financial and Regulatory Analysis Section, Utilities Division

DATE: April 11, 2005

RE: OAK CREEK UTILITY CORPORATION
DOCKET NO. WS-02061A-04-0836

Introduction

Oak Creek Utility Corporation ("Oak Creek" or "Company") separately and concurrently filed applications for a permanent rate increase and a request for authority to issue \$40,000 of promissory notes and other evidences of indebtedness payable at periods of more than twelve months after the date of issuance with the Arizona Corporation Commission ("Commission") on November 19, 2004.

On March 17, 2005, Oak Creek filed a motion to consolidate the rate case and the financing case. Staff did not oppose the consolidation motion.

Notice

Oak Creek filed an Affidavit of Mailing to certify that it sent a Notice to Customers, by first class mail, to all customers of record as of November 1, 2004, regarding its request to incur debt.

Background

Oak Creek was formed in 1985 as a for-profit Arizona perpetual corporation. Oak Creek is located in Coconino County, Arizona, on the east side of Oak Creek along Highway 89A. The Company serves a 6.63 acre certificated area and has about 30 metered customers.

Purpose of Financing

The Arizona Department of Environmental Quality ("ADEQ") found Oak Creek to be in violation of A.A.C. R-18-4-503(A), failure to provide minimum storage requirements for a community water system. Oak Creek proposes to use the proceeds of the \$40,000 loan to comply with ADEQ requirements. Oak Creek also asks that authorization be given for the reasonable charging of loan funds to operating expenses or income.

Description of Proposed Financing

The Company proposes a \$40,000 twenty-year fully amortizing loan from the Water Infrastructure Finance Authority ("WIFA") at 6.00 percent with monthly debt service of \$286.57.

Engineering Analysis

Staff reviewed the proposed water storage tank and facilities plans and concludes that the capital improvement projects are appropriate and that the estimated costs are reasonable.

Financial Analysis

Schedule DRR-1 presents historical financial information for the Water and Wastewater Divisions combined for the year ended December 31, 2003, in Column A. Column B presents pro forma financial information as recommended by Staff in the rate case and the inclusion of a \$40,000 loan over twenty years at 6.00 percent that provides for a 0.575 percent cushion over the March 30, 2005 interest rate of 5.425 percent. The latter represents the current prime rate of 5.75 percent plus 2 percent times the current subsidy rate of 70 percent $[(5.75\% + 2\%) \times .7]$. The subsidy rate may differ slightly at loan closing.

The pro forma financial information results in times interest earned ratio ("TIER") and debt service coverage ratio ("DSC") of 4.78 and 4.31, respectively.

TIER represents the number of times earnings cover interest expense on long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not mean that debt obligations cannot be met in the short term.

DSC represents the number of times internally generated cash will cover required principal and interest payment on long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations. A DSC less than 1.0 means that debt service obligations cannot be met by cash generated from operations and that another source of funds is needed to avoid default.

Schedule DRR-1 shows that the Company had a negative equity position at December 31, 2003. Normally, it would be inappropriate for an entity with negative equity to obtain new debt. However, the Company has no known ability to obtain the equity capital it requires to fund plant

improvements to comply with ADEQ requirements and to provide adequate service. Therefore, it is in the public interest for the Company to obtain a loan for the designated purposes since the pro forma TIER and DSC show good ability to service the proposed debt, and the loan is its best (only) alternative for obtaining the needed funds.

Staff Conclusions and Recommendations

Staff concludes that the \$40,000 expenditure is necessary to expand storage facilities to serve present customers and to comply with ADEQ requirements.

Staff further concludes that its recommended rates in the pending rate case provide sufficient debt service capacity for the proposed \$40,000 loan.

Staff further concludes that use of loan proceeds for operating expenses or income is an inappropriate use of the funds.

Staff further concludes that issuance of debt in the amount of \$40,000 is within Oak Creek's corporate powers, compatible with the public interest, compatible with sound financial practices, and will not impair its ability to perform service.

Staff recommends authorization to obtain \$40,000 of long-term debt financing on the terms and conditions consistent with or better than those used in Staff's pro forma analysis subject to establishment of rates that provide Staff's recommended operating income.

Staff further recommends approval of granting of liens in favor of the lender as required to secure the borrowings authorized.

Staff further recommends denial of Oak Creek's request to use loan funds for operating expenses or income.

Staff further recommends authorizing Oak Creek to engage in any transaction and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends that Oak Creek be ordered to file copies of all executed financing documents with Docket Control within 90 days of loan closing.

Oak Creek Water and Wastewater Divisions Combined

Docket No. WS-02061A-04-0836

Test Year Ended December 31, 2003

Schedule DRR-1

FINANCIAL ANALYSIS

Selected Financial Data
Including Immediate Effects of the Proposed Debt

		[A] <u>12/31/2003</u>		[B] <u>Pro Forma</u>	
1	Operating Income	\$ (9,673)		\$ 11,329	
2	Depreciation & Amort.	3,527		3,504	
3	Income Tax Expense	0		0	
4					
5	Interest Expense	0		2,371	
6	Repayment of Principal	0		1,068	
7					
8					
9	TIER				
10	[1+3] ÷ [5]	N/A		4.78	
11	DSC				
12	[1+2+3] ÷ [5+6]	N/A		4.31	
13					
14					
15					
16					
17					
18	Short-term Debt	\$0	0.0%	\$1,068	34.5%
19					
20	Long-term Debt	\$0	0.0%	\$38,932	1,259.1%
21					
22	Common Equity	(\$36,908)	100.0%	(\$36,908)	-1,193.7%
23					
24	Total Capital	(\$36,908)	100.0%	\$3,092	100.0%
25					
26					
27					